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Cases, Regulations and Statutes

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made available through I.R.C. § 642(h), the amount in excess of the gross income is not deductible by the income beneficiary or beneficiaries of the trust.[20] However, if the trust also terminates *during the taxable year in which it is allowed the Section 642(h) deductions,* the deductions in excess of gross income are available to the remainder holders succeeding to the property.[21] Again, the deductions would be allowable to "beneficiaries succeeding to the property of the trust" but not to those with a mere income interest.[22]

What if a trust beneficiary has the power to terminate the trust and, in fact, does so, in whole or in part, during the taxable year in which it is allowed the deductions allowed under *I.R.C. § 642(h)?* It would seem that the deductions should be allowed to the trust to that extent.

Excess deductions as itemized deductions

It appears that the beneficiaries can claim the deductions only for the taxable year in which or with which the trust (or estate) terminates. If the deductions exceed the gross income, the excess may be carried over to a later year.[23] Unused excess deductions for some expenses may be subject to the two percent floor.[24] The future of the proposed regulations remains unclear inasmuch as the proposed regulations were issued before the Supreme Court decision in *Rudkin*. Thus, excess deductions subject to the two-percent limit can be taken only to the extent that a beneficiary's total miscellaneous itemized deductions exceed two percent of the beneficiary's adjusted gross income *if the deductions are subject to the two percent limitation.*

Passive activity losses

Passive activity losses distributed by an estate or trust are not allowable as a deduction ". . . for any taxable year."[25] Rather, the income tax basis of the interest distributed is increased by the amount of the passive activity losses allocable to that interest.[26]

ENDNOTES

[1] I.R.C. § 172.

[2] I.R.C. § 1222.

[3] I.R.C. § 642(h).

[4] Rev. Rul. 57-31, 1957-1 C.B. 201. See generally 2 Harl, *Farm Income Tax Manual* § 4.03 (2010 ed.).

[5] I.R.C. § 172.

[6] I.R.C. § 1212.

[7] I.R.C. § 642(h).

[8] I.R.C. §§ 642(b), 642(h)(2).

[9] I.R.C. §§ 642(c), 642(h)(2).

[10] I.R.C. § 642(h).

[11] See notes 8 and 9 *supra*.

[12] I.R.C. § 642(h).

[13] See Treas. Reg. § 1.642(h)-3.

[14] Rev. Rul. 60-134, 1960-1 C.B. 259.

[15] Treas. Reg. § 1.642(h)-3.

[16] Rev. Rul. 60-134, 1960-1 C.B. 259.

[17] I.R.C. § 642(h).

[18] Rev. Rul. 57-31, 1957-1 C.B. 201.

[19] 1957-1 C.B. 201.

[20] Rev. Rul. 57-31, 1957-1 C.B. 201.

[21] I.R.C. § 642(h)(2). See Rev. Rul. 57-31, 1957-1 C.B. 201.

[22] See Treas. Reg. § 1.642(h)-3.

[23] Treas. Reg. § 1.642(h)-2.

[24] I.R.C. § 67. See William L. Rudkin Testamentary Trust v. Comm'r, 128 S.Ct. 782 (S. Ct. 2008). See also Prop. Treas. Reg. § 1.67-4(a).

[25] I.R.C. § 469(j)(12).

[26] *Id*.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

BANKRUPTCY

FEDERAL TAX

DISCHARGE. The debtor owed taxes for 1998-2006 and sought to have the taxes declared dischargeable in a bankruptcy case filed in 2009. The debtor filed all the returns late, filed multiple bankruptcy cases from 2005 through the present case, made several low offers in compromise, provided false information to the IRS, placed assets in the names of other persons, and initiated several other tax proceedings. The debtor was employed during these years and had ample income to pay the taxes but spent the money on a residence and placed funds in a retirement account. The court found that the debtor had done most of these activities with the intent to hinder or delay the IRS collection of the taxes owed; therefore, the taxes were nondischargeable under Section 523(a)(1)(C) for willful attempts to evade or defeat taxes. ***In re* Acker, 2010-2 U.S. Tax Cas. (CCH) ¶ 50,636 (E.D. Texas 2010)**.

FEDERAL FARM PROGRAMS

FARM LOANS. The FSA has issued proposed regulations amending the Farm Loan Program loan making regulations to implement four provisions of the Food, Conservation, and Energy Act of 2008 (2008 Farm Bill). The proposed amendments rename, expand, and make permanent the Beginning Farmer and Rancher Land Contract Guarantee Pilot Program. The proposed amendments also change the farm experience requirements in the regulations for direct Farm Operating Loans and direct Farm Ownership Loans and make some equine farmers and certain equine losses eligible for Emergency Loans. **75 Fed. Reg. 57866 (Sept. 23, 2010)**.

TUBERCULOSIS. The APHIS has issued interim regulations amending the bovine tuberculosis regulations reclassifying the zone consisting of an area in the northwest corner of Minnesota as a modified accredited advanced zone, and the zone comprising the remainder of Minnesota as an accredited-free zone. **75 Fed. Reg. 60586 (Oct. 1, 2010)**.

FEDERAL ESTATE AND GIFT TAXATION

ADMINISTRATIVE EXPENSES. The estate had successfully adjudicated a refund for federal estate taxes, *Keller v. United States, 2009-2 U.S. Tax Cas. (CCH) ¶ 60,579 (S.D. Texas 2009)*, and filed claims for deduction for administrative expenses for accounting and legal services. The court allowed the deduction for the claims except to the extent the claims were for contingency fees and future work because the court found these services not necessary for the administration of the estate. **Keller v. United States, 2010-2 U.S. Tax Cas. (CCH) ¶ 60,606 (S.D. Texas 2010)**.

CREDIT FOR PRIOR TRANSFERS. The decedent's predeceased spouse died less than three months before the decedent died. The predeceased spouse's estate filed its estate tax return just over one month before the decedent's estate's return was filed. The decedent's estate claimed a deduction for the federal and state estate taxes. Although the IRS agreed that the decedent's estate was eligible for the prior transfer credit under I.R.C. § 2013, the parties disagreed as to the calculation of the credit and whether the credit included the state estate taxes paid by the predeceased decedent's estate. The decedent's estate argued that the credit equaled all the federal and state estate taxes and the IRS argued that the credit was limited by I.R.C. § 2013(b) and (c). Section 2013(b) limits the credit to the amount which equals the value of transferred property multiplied by the transferor's adjusted federal estate tax divided by the transferor's adjusted taxable estate. For purposes of this limitation, the phrase "adjusted federal estate tax" means the amount of federal estate tax paid with respect to the transferor's estate plus certain credits allowed the transferor's estate. The phrase "transferor's adjusted taxable estate" means the amount of the transferor's taxable estate decreased by the amount of any "death taxes," including federal and state estate taxes, paid with respect to the transferor's gross estate. Unser Section 2013(c) the credit is limited to the difference between (1) the net estate tax payable with respect to the decedent's estate, determined without regard to any credit under section 2013, and (2) the net estate tax determined as described immediately above but computed by subtracting from the decedent's gross estate the value of the property transferred adjusted by any charitable deduction, if applicable. The credit is limited to the lesser of the two limitations. The court held that, in the calculation under the first limitation, the predeceased decedent's taxable estate was not reduced by the applicable credit amount. The court disallowed any prior transfer credit for state estate taxes paid by the predeceased decedent's estate because I.R.C. § 2013 had no provision for such a credit. The court also disallowed any deduction for the decedent's estate for payment of the federal and estate taxes by the predeceased decedent's estate under I.R.C. § 2053. **Estate of Le Caer v. Comm'r, 135 T.C. No. 14 (2010)**.

DISCLAIMERS. The decedent's will included a bequest to an heir of a portion of the residuary estate. The will provided that, if the heir predeceased the decedent, the heir's share would pass to the heir's children. The heir disclaimed the bequest and the property in the form of stock in several corporations, was transferred to the heir's children. The IRS determined that, under Mississippi law, the disclaimed interest would not pass under the will but would pass under intestacy law because the will had no provision for passage of disclaimed property. The court agreed with the IRS interpretation of Mississippi law and ruled that the disclaimed stock passed by intestacy back to the heir; therefore, the subsequent transfer of the stock to the children was a taxable gift. **Estate of Tatum v. United States, 2010-2 U.S. Tax Cas. (CCH) ¶ 60,607 (S.D. Miss. 2010)**.

GENERATION-SKIPPING TRANSFERS. The grantor had established an irrevocable trust prior to September 25, 1985 which now had five beneficiaries. The trustee obtain court permission to modify the trust to allow for distributions of trust corpus to a beneficiary for the "reasonable care, maintenance, or education, or on account of any illness, infirmity, or other life emergency." The trustee also obtained court permission to divide the trust into five pro rata trusts, one for each beneficiary. The IRS held that the modification of the trust and the division of the trust did not subject the trust to GSTT. **Ltr. Rul. 201039003, June 25, 2010**.

FEDERAL INCOME TAXATION

AMORTIZATION. The taxpayer purchased a vineyard which was located in two viticultural areas designated as American viticultural area (AVA) by the Alcohol and Tobacco Tax and

Trade Bureau ("TTB") of the United States Department of the Treasury under 27 C.F.R. § 9.11. In a Chief Counsel advice letter, the IRS ruled that a portion of the purchase price could be allocated to the right to use the AVA designation and that amount was amortizable as an intangible under I.R.C. § 197. The IRS reasoned that the AVA designation would come from the crop produced on the land and not result from any condition of the land itself. The IRS cautioned that the valuation of the amortizable interest would be difficult because other vineyards in the same area would also have the benefit from the AVA designation. **CCA Ltr. Rul. 201040004, June 24, 2010**.

CAPITAL GAINS. The taxpayer had developed a method of transferring liquids from a vial directly to a medical syringe and had obtained a patent on the method. The taxpayer sold the patent to a medical equipment company for "$1 and for other good and valuable consideration." Four months later, the taxpayer entered into a sales employment agreement with the medical equipment company. The taxpayer claimed the income from the employment as long-term capital gain from the sale of the patent but the IRS re-characterized the income as ordinary income from the employment. The court noted that the taxpayer had no evidence that the employment agreement was tied in anyway to the sale of the patent or that the employment had anything to do with the equipment company's sale or use of the patent. Therefore, the employment income was not compensation for the patent and was properly characterized as ordinary income. **Farris v. Comm'r, T.C. Memo. 2010-222**.

CASUALTY LOSSES. The IRS has issued procedures which enable affected taxpayers to treat damages from corrosive drywall as a casualty loss and provides a "safe harbor" formula for determining the amount of the loss. In numerous instances, homeowners with certain imported drywall have reported blackening or corrosion of copper electrical wiring and copper components of household appliances, as well as the presence of sulfur gas odors. The procedure provides the following relief: (1) Individuals who pay to repair damage to their personal residences or household appliances resulting from corrosive drywall may treat the amount paid as a casualty loss in the year of payment. (2) Taxpayers who have already filed their income tax return for the year of payment generally have three years to file an amended return and claim the deduction. The amount of a loss that may be claimed depends on whether the taxpayer has a pending claim for reimbursement (or intends to pursue reimbursement) of the loss through property insurance, litigation or otherwise. (3) In cases where a taxpayer does not have a pending claim for reimbursement, the taxpayer may claim as a loss all un-reimbursed amounts paid during the taxable year to repair damage to the taxpayer's personal residence and household appliances resulting from corrosive drywall. (4) If a taxpayer does have a pending claim (or intends to pursue reimbursement), a taxpayer may claim a loss for 75 percent of the un-reimbursed amount paid during the taxable year to repair damage to the taxpayer's personal residence and household appliances that resulted from corrosive drywall. A taxpayer who has been fully reimbursed before filing a return for the year the loss was sustained may not claim a loss. A taxpayer who has a pending claim for reimbursement (or intends to pursue reimbursement) may have income or an additional deduction in subsequent taxable years depending on the actual amount of reimbursement received. For purposes of the procedure, the term "corrosive drywall" means drywall that is identified as problem drywall under the two step identification method published by the Consumer Products Safety Commission and the Department of Housing and Urban Development in their interim guidance dated January 28, 2010. **Rev. Proc. 2010-36, I.R.B. 2010-42**.

The taxpayers, husband and wife, owned and operated a construction company. The taxpayers purchased a cabin and surrounding property and leased the property to their church for use as a teen camp, men's retreat and women's retreat. Although there was a written lease, the lease contained no rental terms or firm obligations and no rent was charged. The cabin and contents were damaged in a fire and the taxpayers claimed a casualty loss deduction. The court held that the losses were not deductible under I.R.C. § 165(c)(1) because the property was not operated as a trade or business nor under I.R.C. § 165(c)(2) because the property was not operated with an intent to make a profit. The loss was not eligible for a personal casualty loss because it did not exceed 10 percent of the taxpayers' adjusted gross income. **Sandoval v. Comm'r, T.C. Memo. 2010-208**.

CHARITABLE DEDUCTION. The taxpayer purchased two properties in an historic district in Washington, D.C. and granted a facade conservation easement for both properties to a charitable organization. The taxpayer claimed a deduction for the loss of value to the properties. The taxpayer offered four appraisal reports but only one appraiser testified. That appraiser prepared an appraisal report four years after the grant of the easements and admitted to unfamiliarity with the IRS regulations for a qualified appraiser report and the appraisal had several errors and deficiencies under the regulations. No testimony was provided from the persons who prepared appraisals contemporaneous with the grant of the easements. The court held that the taxpayer failed to provide sufficient evidence of the difference in value of the proeprties before and after the grants of easement; therefore, the disallowance of the deduction was upheld. **Evans v. Comm'r, T.C. Memo. 2010-207**.

CORPORATIONS.

RETURNS. The IRS has issued proposed amendments to the regulations under I.R.C. § 6012 relating to the returns of income corporations are required to file. The proposed regulations require certain corporations to file a report of uncertain tax positions. *75 Fed. Reg. 54802 (Sept. 9, 2010)*. The IRS has announced that a final schedule and instructions are being released. In addition, the IRS is also releasing a directive regarding implementation of Schedule UTP and related matters, and a separate announcement regarding modifications that will be made to the existing Policy of Restraint in conjunction with implementation of Schedule UTP. Based on comments received by the IRS, the final schedule and instructions make a number of significant changes to the April 2010 draft in order to address burden and other concerns expressed by commentators. Some of the major changes include:

• a five-year phase-in of the reporting requirement based on a corporation's asset size;

• no reporting of a maximum tax adjustment;

• no reporting of the rationale and nature of uncertainty in the concise description of the position; and

• no reporting of administrative practice tax positions.

• removal of requirement to include rationale and nature of uncertainty in concise description of the position. **Ann. 2010-75, 2010-2 C.B. 428**.

The IRS has announced that the IRS is expanding its policy of restraint in connection with its decision to require certain corporations to file Schedule UTP, Uncertain Tax Position Statement, and will forgo seeking particular documents that relate to uncertain tax positions and the workpapers that document the completion of Schedule UTP. **Ann. 2010-76, 2010-2 C.B. 432**.

DEPENDENTS. In a Chief Counsel Advice letter, the IRS ruled that a domestic partner who is a dependent of an employee under I.R.C. § 152, is also a dependent for FUTA purposes. **CCA Ltr. Rul. 201040012, Sept. 8, 2010**.

The taxpayer claimed two children as dependents on a return using the head of household status. The one child was a minor and lived with the taxpayer's former spouse. The divorce decree did not allocate the use of the dependency exemption and the former spouse did not agree to allow the taxpayer to use the exemption. The former spouse claimed the child as a dependent. The other child was age 30 and had income of over $13,000. The court held that the taxpayer was not entitled to claim either child as a dependent because (1) the taxpayer failed to prove that the young child lived with the taxpayer for more than one-half of the year and (2) the older child exceeded the age and income limitations for dependents. **Louis v. Comm'r, T.C. Memo. 2010-217**.

DISASTER LOSSES. On September 28, 2010, the President determined that certain areas in the U.S. Virgin Islands are eligible for assistance from the government under the Disaster Relief and Emergency Assistance Act (42 U.S.C. § 5121) as a result of a Hurricane Earl, which began on August 29, 2010. **FEMA-1939-DR.** Accordingly, taxpayers in the areas may deduct the losses on their 2009 federal income tax returns. See I.R.C. § 165(i).

EMPLOYEE EXPENSES. The IRS has announced an update of the simplified per diem rates that employers (or their agents or third parties) can use to reimburse employees for lodging, meals and incidental expenses incurred on or after October 1, 2010 during business travel away from home without the need to produce receipts. The simplified "high-low" per diem rates have decreased to $233 for high-cost localities and decreased to $160 for localities within CONUS. For purposes of applying the high-low substantiation method and the 50-percent limitation on meal expenses, the federal meal and incidental expense rate is treated as $65 for a high-cost locality and $52 for any other locality within CONUS. **Rev. Proc. 2010-39, I.R.B. 2010-42, *superseding*, Rev. Proc. 2009-47, 2009-2 C.B. 524**.

INNOCENT SPOUSE. The taxpayer filed for equitable innocent spouse relief, under I.R.C. § 6015(f), from joint tax liabilities created by the taxpayer's and spouse's joint income tax returns. The IRS denied equitable innocent spouse tax relief under Treas. Reg. § 1.6015-5(b)(1) because the relief was requested more than two years after collection efforts had begun. The court discussed the recent case of *Lantz v. Comm'r, 2010-1 U.S. Tax Cas. (CCH) ¶ 50,446 (7th Cir. 2010), rev'g and rem'g, 132 T.C. 131 (2009),* under which the appellate court upheld the imposition of a two-year limitation period for requests for equitable innocent spouse relief. Reiterating its decision in *Lantz*, the Tax Court held that, although I.R.C. § 6015(b) and (c) have a two-year limitation period, the absence of a two year limitation period in I.R.C. § 6015(f) indicated Congress' intent to allow equitable relief requests to be made for a longer, if not unlimited, period. Therefore, the court held that the two year period of limitations in Treas. Reg. § 1.6015-5(b)(1) was invalid as to requests for equitable innocent spouse relief under I.R.C. § 6015(f). This case is appealable to the Sixth Circuit Court of Appeals. **Hall v. Comm'r, 135 T.C. No. 19 (2010)**.

While the taxpayer was married, the taxpayer's spouse owned all the business assets and controlled all the financial affairs of the couple. The spouse had all the federal tax returns prepared and the taxpayer signed them without determining their accuracy. The taxpayer claimed that the taxpayer had no knowledge that taxes were not being paid. The taxpayer and spouse divorced and soon after the spouse died, the taxpayer filed for equitable innocent spouse relief. The IRS denied relief on the basis that the taxpayer did not show that the taxpayer had no knowledge that the taxes would not be paid and that the taxpayer would suffer economic hardship from paying the taxes. The court held that equitable innocent spouse relief should have been granted because (1) the taxpayer's lack of knowledge of the couple's finances prevented the taxpayer from knowing that the taxes would not be paid, and (2) the taxpayer had demonstrated that the taxpayer's current income did not exceed the taxpayer's reasonable living expenses. **Harper v. Comm'r, T.C. Summary Op. 2010-153**.

INVOLUNTARY CONVERSIONS. The IRS has issued guidance on determining the replacement period for application of I.R.C. § 1033(e) to the sale of livestock sold on account of drought. *Notice 2006-82, 2006-2 C.B. 529*. Under that guidance, under I.R.C. § 1033(e)(2)(B), the standard replacement period (four years after the close of the first taxable year in which any part of the gain from a drought sale occurs) can be extended by the Secretary of the Treasury if the Secretary determines that the drought area was eligible for federal assistance for more than three years. The IRS, after consultation with the National Drought Mitigation Center, publishes in September of each year a list of counties for which exceptional, extreme, or severe drought was reported during the preceding 12 months. Taxpayers may use this list instead of U.S. Drought Monitor Maps to determine whether a

12 month period ending on August 31 of a calendar year includes any period for which exceptional, extreme, or severe drought is reported for a location in the applicable region. The IRS has published a list of the counties and parishes in the United States that have suffered exceptional, severe or extreme drought during the 12 months ending August 31, 2010, sufficient to extend the livestock replacement period. **Notice 2010-64, 2010-2 C.B. 421**.

PASSIVE ACTIVITY LOSSES. The taxpayer was employed full-time at a nuclear power plant. The taxpayer owned four residential rental properties which the taxpayer managed during non-working hours. The taxpayer treated the four properties as one activity and claimed a loss deduction related to the rental properties on Schedule E but the IRS disallowed most of the loss deduction. The taxpayer argued that the taxpayer qualified for the I.R.C. § 469(c)(7)(B)(ii) exception for real estate professionals. The taxpayer presented evidence of 645 hours spent on the activities and argued that the number of hours spent on the rental activity included additional hours spent "on-call" for work on the properties when the taxpayer was not working at the taxpayer's full-time job. The court held that the "on-call" time could not be included because no services were performed on the rental properties. The taxpayer was allowed only a portion of the $25,000 exception under I.R.C. § 469(i) because the taxpayer's gross income exceeded $100,000. **Moss v. Comm'r, 135 T.C. No. 18 (2010)**.

PENSION PLANS. For plans beginning in October 2010 for purposes of determining the full funding limitation under I.R.C. § 412(c)(7), the 30-year Treasury securities annual interest rate for this period is 4.28 percent, the corporate bond weighted average is 6.21 percent, and the 90 percent to 100 percent permissible range is 5.59 percent to 6.21 percent. **Notice 2010-70, I.R.B. 2010-44**.

QUALIFIED MORTGAGE INTEREST. An individual taxpayer purchased a principal residence for $1.5 million, with $300,000 cash and a $1.2 million mortgage loan. The IRS ruled that the first $1 million of debt was qualified acquisition indebtedness for which interest was eligible for the residential mortgage interest deduction. The IRS also ruled that the interest on an additional $100,000 of indebtedness was eligible for the deduction as home equity indebtedness interest because the indebtedness was not considered acquisition indebtedness under I.R.C. § 163(h)(3)(B):

> "(B) Acquisition indebtedness
> (i) In general
> The term ''acquisition indebtedness'' means any indebtedness which -
> (I) is incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer, and
> (II) is secured by such residence."

However, the IRS does not fully explain why the first $100,000 of indebtedness above $1 million is not considered acquisition indebtedness. The IRS merely states that the definition of home equity indebtedness does not require that the indebtedness not be used to acquire the residence. This appears to contradict the statute which excludes acquisition indebtedness from the definition of home equity indebtedness. See I.R.C. § 163(h)(3)(C):

> "(C) Home equity indebtedness
> (i) In general
> The term ''home equity indebtedness'' means any indebtedness (other than acquisition indebtedness) secured by a qualified residence to the extent the aggregate amount of such indebtedness does not exceed -
> (I) the fair market value of such qualified residence, reduced by
> (II) the amount of acquisition indebtedness with respect to such residence.

Query: It appears that the IRS sees only the first $1 million as acquisition indebtedness, with any additional indebtedness as other than acquisition indebtedness, thus opening up the additional indebtedness for qualification for home equity indebtedness. The interest on the remaining $100,000 of indebtedness was considered personal interest and was not deductible. The IRS acknowledged that this ruling was contrary to the holdings in *Pau v. Comm'r, T.C. Memo. 1997-43* and *Catalano v. Comm'r, T.C. Memo. 2000-82, rev'd on other grounds, 279 F3d 682 (9th Cir. 2002)*. **Rev. Rul. 2010-25, I.R.B. 2010-44**.

RETURNS. The IRS has announced that individual and business taxpayers will no longer receive paper income tax packages in the mail from the IRS. These tax packages contained the forms, schedules and instructions for filing a paper income tax return. The IRS is taking this step because of the continued growth in electronic filing and the availability of free options to taxpayers, as well as to help reduce costs. In early October, the IRS will send a postcard to individuals who filed paper returns last year and did not use a tax preparer or tax software. The information will explain how to get the tax forms and instructions they need for filing their tax year 2010 return. The forms and instructions will be available in early January 2011. **Notice 1400, 1400-A, 1400-J, 1400-E**.

The IRS has published a draft Form W-2 for 2011, which employers use to report wages and employee tax withholding. The IRS also announced that it will defer the new requirement for employers to report the cost of coverage under an employer-sponsored group health plan, making that reporting by employers optional in 2011. The draft Form W-2 includes the codes that employers may use to report the cost of coverage under an employer-sponsored group health plan. The Treasury Department and the IRS have determined that this relief is necessary to provide employers the time they need to make changes to their payroll systems or procedures in preparation for compliance with the new reporting requirement. The IRS will be publishing guidance on the new requirement later this year. Although reporting the cost of coverage will be optional with respect to 2011, the IRS continues to stress that the amounts reportable are not taxable. Included in the Affordable Care Act passed by Congress in March 2010, the new reporting requirement is intended to be informational only, and to provide employees with greater transparency into overall health care costs. **Notice 2010-69, I.R.B. 2010-44**.

S CORPORATIONS

ACCOUNTING METHOD. The S corporation taxpayer attached to the federal income tax return, an original Form 3115, Application for Change in Accounting Method, filed under the automatic procedures of *Rev. Proc. 2008-52, 2008-2 C.B. 587, as amplified, clarified, and modified by Rev. Proc. 2009-39, 2009-2 C.B. 371*. The taxpayer filed Form 3115 to change the method of accounting for certain depreciable property. The taxpayer relied on its accounting firm to file a copy of the Form 3115 (with signature) with the IRS national office, but the copy was not filed with the IRS national office as required by section 6.02(3)(a) of *Rev. Proc. 2008-52*. The IRS granted an extension of time to file a copy of From 3115 with the national office. **Ltr. Rul. 201039006, July 1, 2010**.

The taxpayers, husband and wife, were the sole shareholders of two S corporations. The retail corporation sold merchandise acquired from the wholesale corporation. The retail corporation did not pay the wholesale corporation for the merchandise and merely increased its accounts payable. The retail corporation used the accrual method of accounting and the wholesale corporation used the cash method of accounting. The IRS disallowed the retail corporation's use of cost of goods sold because the corporation did not include its sales in income. The IRS sent a notice of deficiency to the taxpayers for a closed tax year, based on the disallowance of the use of cost of goods sold. The court held that the notice was proper in that it was based on an I.R.C. § 481 adjustment in accounting method which was not subject to the limitations of a closed tax year. **Bosamia v. Comm'r, T.C. Memo. 2010-218**.

SHAREHOLDERS. The taxpayer was an S corporation which had a resident alien as a shareholder. The shareholder lost the resident alien status, resulting in termination of the S corporation status. The taxpayer reacquired the shares of the ineligible shareholder and all other shareholders treated the taxpayer as an S corporation. The IRS ruled that the termination was inadvertent and did not result in loss of S corporation status. **Ltr. Rul. 201040001, July 8, 2010**.

TRUSTS. An irrevocable trust was created which provided that, under the trust agreement, whenever a gift was made or was deemed to have been made to the trust during the grantor's lifetime, the beneficiary had the power to withdraw out of the assets of the trust an amount not to exceed the amount of such gift, provided, however, that the amount that could be withdrawn in any one calendar year was limited to the maximum amount as to which the power of withdrawal could lapse without the lapse constituting the release of a general power of appointment under I.R.C. §§ 2041(b)(2) and 2514(e). The IRS ruled that the beneficiary of the trust would be treated as the owner of the trust under I.R.C. § 678 and that the trust was an eligible S corporation shareholder. **Ltr. Rul. 2010-39010, June 29, 2010**.

TAX COURT. The taxpayer received a notice of deficiency on May 12, 2009 but the Tax Court did not receive the filing of a petition until November 12, 2009, 184 days after the notice and well beyond the 90 day appeal period. The taxpayer provided evidence from the postal store that the original petition was timely mailed but was damaged by the Post Office and returned to the taxpayer on November 3, 2009. The taxpayer mailed a new copy three days later. The court held that the taxpayer sufficiently proved a timely mailing of the original petition sufficient to grant jurisdiction in the Tax Court. **Van Brunt v. Comm'r, T.C. Memo. 2010-220**.

TAX RETURN PREPARERS. The IRS has announced a new online application system for tax return preparers to obtain a PTIN is now available. All paid tax return preparers who prepare all or substantially all of a tax return are required to use the new registration system to obtain a PTIN. Access to the online application system will be through the Tax Professionals page of www.IRS.gov. Individuals who currently possess a PTIN will need to reapply under the new system but generally will be reassigned the same number. **IR-2010-099**.

The IRS has adopted as final regulations governing the identifying numbers to be used by tax return preparers on tax returns prepared for other taxpayers. Tax return preparers will need to apply and pay for a preparer tax identification number (PTIN) which may not be the preparer's social security number. In keeping with the announced program to register all tax return preparers who are not attorneys, CPAs, or enrolled agents, only those individuals and registered tax return preparers will be given PTINs. **75 Fed. Reg. 60309 (Sept. 17, 2010)**.

The IRS has adopted as final regulations which impose a $50 user fee on tax return preparers who obtain a new or renewed preparer tax identification number (PTIN). The fee will pay for federal tax compliance and suitability checks to be performed on all individuals who apply for or renew a PTIN. **75 Fed. Reg. 60316 (Sept. 30, 2010)**.

The IRS has announced the delay, until further notice, of the renewal period for enrolled agents whose tax identification number ends in a 4, 5 or 6 that was scheduled to begin on November 1, 2010. The IRS is currently implementing the recommendations in Publication 4832, Return Preparer Review, which was published on January 4, 2010. As part of the implementation, the IRS published regulations that require all individuals who apply for or renew a PTIN to pay a $50 user fee, plus a separate fee of $14.25 to the vendor. The IRS is delaying the upcoming renewal period for these enrolled agents to ensure that the revised user fee to renew enrollment as an enrolled agent is effective before the start of the next renewal period. The IRS will publish a schedule for affected enrolled agents to renew their enrollment in the Internal Revenue Bulletin and on the IRS Office of Professional Responsibility (OPR) webpage (http://www.irs.gov/taxpros/agents/index.html). Once the IRS has determined a date for the renewal period the schedule will be published at least 30 days prior to the beginning of the revised enrollment period and affected enrolled agents will have between 60 and 120 calendar days to submit the required renewal applications. OPR will not accept or process applications for renewal of enrollment until the enrollment renewal period has been announced. This delay will not impact an affected enrolled agent's current status as an enrolled agent in good standing, the number of hours of continuing professional education required for renewal or the time period within which these hours must be completed. **Ann. 2010-81**.

TRADE OR BUSINESS. The taxpayer was employed at a car

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dealership as a sales manager. The taxpayer was able to obtain new cars at a discount, use the cars for personal use and then offer them for sale at a profit. The taxpayer placed a for sale sign on the cars immediately after acquiring them. However, almost all of the cars were traded-in to the dealership for new cars. The taxpayer claimed income and expenses for the purchases and trade-in/sales on Schedule C. The court held that the activity did not amount to a trade or business because the use of the vehicles was for personal use only and the taxpayer did not offer the cars for sale to the public, other than the signs in the cars. **Sada v. Comm'r, T.C. Summary Op. 2010-146**.

TRAVEL EXPENSES. The taxpayer was a plumber/pipefitter and a member of the Washington, D.C. plumbers' union. The taxpayer moved to Florida to live with an ill parent during the tax years involved here. The taxpayer worked on several jobs in a variety of locations in and outside of the Washington area. The taxpayer claimed travel expenses for driving to the jobs from the Florida address. The court held that Washington, D.C. was the taxpayer's tax residence for purposes of the deductibility of the travel expenses because the taxpayer remained a registered member of the local union and obtained several jobs in that area. **Summerfield v. Comm'r, T.C. Summary Op. 2010-143**.

The taxpayer was employed as a heavy equipment operator by two companies at several work sites in the state. The taxpayer claimed Form 2106 employee business expenses for travel and meals. The taxpayer also claimed deductions for work gloves, boots and a cellular telephone. The taxpayer had no written records to substantiate any of the expenses. However, the taxpayer presented records created and maintained by the two employers as to the taxpayer's work periods and locations. The court allowed those records as sufficient substantiation of some of the travel expenses. The deduction for the cell phone was denied for lack of written records. The deduction for the work gloves and boots was reduced because the court felt they exceeded the reasonable costs of those items. **Holland v. Comm'r, T.C. Summary Op. 2010-132**.

TRUSTS. The taxpayer created a qualified personal residence trust which initially provided for distribution of the trust residence to the remainder holders, the grantor's children. The taxpayer obtained a modification of the trust to provide that, upon the termination of the trust, the remainder holders had a power of appointment which could be used to direct the trustee to amend the trust to give the taxpayer a term interest in the trust property as a gift from the remainder holders. The trust terminated and the remainder holders exercised the power of appointment. The IRS ruled that, because the modification was similar to the sample given in Rev. Proc. 2003-42, 2003-1 C.B. 993, Section 4, the modification did not subject the trust to the special valuation rules of I.R.C. § 2701(a)(2). **Ltr. Rul. 201039001, June 28, 2010**.

NEGLIGENCE

RES IPSA LOQUITUR. The plaintiff was injured by falling through a dock on a pond on a farm owned by the defendants. The defendants had the dock removed because it was a hazard and was no longer used. The plaintiff argued that the negligence of the defendant was proved by the doctrine of res ipsa loquitur because the accident would not ordinarily happen without the negligent upkeep by the defendants. The trial court granted summary judgment for the defendants and the lower appeals court upheld the judgment, holding that there were other causes of the accident beyond mere negligence by the defendants. The Washington Supreme court reversed holding that res ipsa loquitur may be used to prove negligence where (1) the accident or occurrence that caused the plaintiff's injury would not ordinarily happen in the absence of negligence, (2) the instrumentality or agency that caused the plaintiff's injury was in the exclusive control of the defendant, and (3) the plaintiff did not contribute to the accident or occurrence. In this case, the court held that the plaintiff had demonstrated that all three elements existed sufficient to prevent summary judgment. **Curtis v. Lein, 2010 Wash. LEXIS 809 (Wash. 2010), *rev'g*, 206 P.3d 1264 (Wash. Ct. App. 2009)**.

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